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THE DAILY NEWSPAPER OF PUBLIC FINANCE

A Call for Enhancement

Frank Urges Federal Guarantee for Munis

Bond Buyer | Thursday, January 15, 2009

By [Andrew Ackerman](#)

WASHINGTON - House Financial Services Committee chairman Barney Frank and Rep. Gerald Connolly, D-Va., yesterday called for Congress to consider legislation that would require the federal government to provide direct credit enhancement or a guarantee for municipal bonds.

They outlined their proposal during a debate by House lawmakers of a bill that would establish conditions for the second \$350 billion portion of the Troubled Assets Relief Program. Frank introduced the TARP legislation on Friday and it is to be voted on today.

Among other things, the legislation would clarify that Treasury has the authority, under the Emergency Economic Stabilization Act, which Congress approved in October to authorize TARP, to purchase municipal bonds or to provide credit enhancement for munis that could be purchased under a Fed program in return for a short-term loan.

The National Association of Counties, led by executive director Larry Naake, and Rep. Robert Andrews, D-NJ, sent letters to Frank applauding the provision. Andrews said \$75 billion of TARP funds should be used to purchase munis.

At press time, members were also considering including in the TARP bill a requirement that the federal government guarantee leaseback deals that transit agencies entered into with private investors and that technically defaulted when the guarantors credit ratings were downgraded below triple-A. However, such a provision would be unlikely to gain support in the Senate where leaders of the Senate Finance Committee, which has jurisdiction over tax issues, have said they would adamantly oppose such a provision.

The transit measure has been aggressively pushed by lobbyists for the transit agencies, which are facing billions of dollars of termination payments from leaseback deals that technically defaulted after their insurers' ratings were downgraded last year.

But Max Baucus, D-Mont., and Charles Grassley, R-Iowa, the ranking members on the Senate Finance Committee, both expressed opposition to the measure when it last surfaced as an addition to auto-maker bailout legislation in December, which passed the House but did not clear the Senate.

Though the TARP legislation does not include a federal guarantee for muni debt, Frank and Connolly used last night's two hours of debate on the measure to propose that a separate bill be drafted to authorize one.

Connolly called for a federal program that would provide direct credit enhancement for munis, or create a federally sponsored insurance entity to insure munis. He said he hoped that such a program would insure market access for municipal debt and reduce the spreads between municipals and Treasuries.

The federal government could also provide a program to repackage muni bonds as Treasury notes that would be guaranteed by the federal government, Connolly said. Payment of interest on such notes would be made by the municipal issuer, though they would appear like normal Treasuries to investors and would be backed by the federal government.

Congressional action is needed because investors have fled to Treasuries and municipal issuers have been shut out of the capital markets, Connolly said.

"This double-whammy has effectively denied many of the 55,000 municipal tax-exempt bond issuers across the nation any ability with which to finance capital projects," he said. "State and local governments are being undervalued. In the context of the stimulus proposal, I would argue that they are the most effective engine for job creation as they are the ones building new schools and fire stations and hiring bus drivers and police officers."

In response, Frank said: "One of the most sympathetic victims of this financial crisis has been the municipalities. Their capacity to finance what's necessary for the quality of life of their constituents has been impaired by factors well beyond their control. We have an obligation to try to come to their aid."

He promised the committee will hold hearings this year on the establishment of some form of federal guarantee for municipal bonds.

Connolly, who succeeded retired Republican Rep. Tom Davis at the start of the new Congress last week, was formerly chairman of triple-A-rated Fairfax County, Va.

In a separate colloquy with Frank last night, Rep. Gwen Moore, D-Wis., called for the Treasury Department to consider using the TARP funds to purchase mortgage revenue bonds sold by state housing finance agencies, which she noted have been shut out of the credit markets like other municipal issuers.

She asked Frank if his legislation would authorize such purchases. "Aid to municipal finance, and housing as part of that, is clearly included," he replied.

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